FUTURE DEFENCE REVIEW
Working Paper Number 1 Royal United Services Institute July 2009

RUSI
www.rusi.org

Preparing for the Lean Years

Malcolm Chalmers

Future Defence Review Working Papers

This series provides independent analysis and opinion on issues that are likely to feature in a Future Defence Review.

It seeks to promote a vigorous and comprehensive debate, unconstrained by any preconceptions of Britain's role in the world or the purposes of its armed forces, amongst political parties, the academic community, industry and the electorate as a whole.

Related analysis: www.rusi.org/fdr

Defence Budget Crisis
Bill Kincaid

Spending Review
David Kirkpatrick

Global Economic Recession
Ron Smith & Jeffrey Bradford

Defence Inflation
Malcolm Chalmers

Issue

How will British defence spending fare in an age of austerity?

Context

The core defence budgets for 2009/10 and 2010/11 have already been set, and are unlikely to be substantially altered. But, in the immediate aftermath of the next election, most analysts now expect there to be a new comprehensive spending review, leading to a prolonged period of public austerity, including in defence.

Key Findings

- If the MoD's current and capital budgets are reduced in line with those for the whole government (excluding interest payments and social security), total defence spending would fall by an estimated 6.8% in real terms between 2010/11 and 2013/14. The estimated reduction over the six years to 2016/17 would be 11% in real terms.

- If the MoD succeeds in obtaining an exemption from the full impact of planned capital cuts, it could face pressure from another source. Assuming, for example, that health and education are given special treatment and their budgets are frozen at 2010 levels in real terms, and that the rate of growth in social security spending is reduced to 1% per year, this would leave the rest of government, including the MoD, facing a cut of 14% in their budgets over the period from 2010 to 2016.

- The paper's best estimate is that the MoD will be required to make a real terms budget reduction over the period 2010/16 of around 10-15% in real terms. However, if the government decides to provide even a modest level of real terms growth to health and education, or if the economy fails to recover its previous trend rate of growth by 2010, even tax increases may not be able to prevent even deeper defence spending reductions.

Analysis

If a major review of defence commitments and programmes takes place after the next General Election, as is widely expected, it will do so in very different circumstances from the Strategic Defence Review (SDR), conducted by the incoming Labour government in 1997-98.

The decade after the SDR coincided with a period of sustained economic success, in which ambitious government domestic objectives (notably in relation to health, education and poverty reduction) were funded by buoyant tax revenues. It also saw a marked shift towards a more ambitious and globalist, defence policy, in which the UK armed forces were deployed on major operations to an extent not seen since the 1950s. These interventions were supported by the largest real increase in defence spending since the early 1980s.

The next Defence Review, by contrast, will be overshadowed by the aftershock from the 2008 financial crisis. Latest projections suggest that the UK could be heading for a 2010 fiscal deficit amounting to a breathtaking 14 per cent of GDP, the highest of any OECD economy.[1] Even if the economy quickly recovers its pre-crisis growth rate, a prolonged period of austerity in public expenditure (including defence) now appears inevitable.

The necessity for a period of retrenchment has an additional resonance in relation to military operations. The political consensus on defence policy has been severely strained over the last decade, to an extent not seen since the short-lived Suez adventure of 1956, by the controversies surrounding the two interventions in Iraq and Afghanistan. While strong support remains for fulfilling existing commitments in Afghanistan, there is now a significant shift in attitudes amongst political elites away from the liberal interventionism of the last decade, and towards a more cautious approach to 'wars of choice', especially when the costs of the latter are likely to be high.

The Years of Plenty

The 1998 SDR is widely seen as having been one of the UK's most successful defence reviews. After being in the political wilderness for seventeen years, the New Labour government that came to office in 1997 was committed to showing that it could be taken seriously on defence matters, and that it had learnt the lessons of its flirtation with unilateralist and anti-European policies during the 1980s. Prime Minister Tony Blair appointed one of Labour's most experienced foreign policy experts, George Robertson, to the post of Defence Secretary. From this position, Robertson presided over a major review of defence commitments, the results of which were published in July 1998.[2]

While the SDR did involve significant economies in some areas, it also announced significant enhancements, including the creation of new joint structures and the purchase of two large aircraft carriers. In the decade that followed, the numerical strength of the armed forces continued to fall, as did the numbers of deployed ships, aircraft and armoured vehicles. But this was combined with a programme of substantial qualitative improvement, in which the fruits of previous investments were realised and further capital spending was undertaken. As a result, today's military force structure is still recognisably the one mapped out in the SDR, albeit smaller than was then planned.

This achievement was all the more impressive because the Ministry of Defence (MoD) had to manage its activities within a modest rate of budgetary growth. The New Labour government accepted the tight spending settlement for 1997/98 and 1998/99 that it inherited from the previous government. Thereafter, however, it continued to give defence a relatively low budgetary priority, as Table 1 makes clear. Over the ten years to 2008/09, defence spending in real terms rose by 19 per cent. But most of this increase was a result of the additional costs of operations in Iraq and Afghanistan, totalling £4.5 billion in 2008/09.[3] 'Core' defence spending (excluding operational costs) rose by only 5 per cent in real terms over the decade: an annual rate of increase amounting to a modest 0.5 per cent.

Spending on other major government services increased much more rapidly. The budget for social protection rose by 39 per cent in real terms over the decade, public order and safety took an additional 50 per cent, education spending increased by 63 per cent, and the health service enjoyed a massive 85 per cent increment in its real resources. The Labour government has therefore presided over a major shift of spending priorities away from defence.

If one compares this record with that of the Conservatives in the past, a considerable degree of continuity is apparent. While the percentage increase in total government spending has increased sharply – from only 2 per cent over Mrs Thatcher's last seven years, to 14 per cent during the years 1990-98, to 48 per cent over 1998-2008 – the relative priority given to the major departments within this total has remained relatively stable. (See Table 1) The NHS has remained consistently the top priority for both parties, rising from 123 per cent of the defence budget in 1990-91 to 298 per cent in 2008-09. Public order (police, prisons, courts, and fire services) was given a relatively higher priority under the Conservatives, while Labour has given greater priority to education. During the last decade, both public order and education have enjoyed real increases of 50-60 per cent in their budgets, compared to the relatively modest 19 per cent increase for defence. Social

protection spending (pensions, support for families, the disabled and unemployed) has remained the single largest element in the total budget, though its relative priority has declined somewhat in recent years.

The low level of growth in defence spending since the end of the Cold War has allowed a significant 'peace dividend' to be realised, as a result of which spending in other areas has been higher (and/or taxation levels have been lower) than would otherwise have been possible. One way of calculating the size of this 'dividend' is to estimate what the defence budget would have been had it grown at the same rate as the rest of public spending. On this basis, defence spending in 2008/09 would have reached £61 billion, a full £25 billion higher than its actual level.

Yet the low priority given to defence spending is not only a post-Cold War phenomenon. During the seven years prior to the end of the Cold War, under Mrs Thatcher's premiership, defence spending fell by 7 per cent in real terms. Over the same period, by contrast, spending on law and order rose by 36 per cent, health by 20 per cent, education by 13 per cent, and social security spending rose by 9 per cent.[4] Indeed, in the entire period since the death of Stalin in 1953, the only sustained period in which the defence budget has grown at a rate comparable with that of total government spending has been in the six years after 1978/79, a consequence of the UK's commitment (under Prime Ministers Callaghan and Thatcher) to the NATO 3 per cent target for annual real spending increases.

Growing Stresses

Over the last ten years, defence planners have sought to meet the demands generated by new interventions despite being provided with only limited increases in their core budget. They have

Table 1: UK Defence Spending in Historic Context, 1983/84 to 2008/09

	1983-1990 (Thatcher)	1990-98 (Major)	1998-2008 (Blair)
Health	+20%	+36%	+85%
Education	+13%	+12%	+63%
Public order & safety	+36%	+21%	+50%
Social protection	+ 9%	+33%	+39%
Defence	-7%	-12%	+19%
Debt interest	-9%	+12%	-15%
Total Managed Expenditure	+2%	+14%	+48%

Sources: HM Treasury, *Public Expenditure Statistical Analyses 1999-2000*, Cm 4201, March 1999, Table 4.3; HM Treasury, *Public Expenditure Statistical Analyses 2009*, Cm 7630, June 2009, Table 4.3. All in constant prices.

managed to do this, in part, through continuing economies in legacy capabilities, seen as less relevant to the post-Cold War world. They have also drawn increasingly from the Treasury Reserve to fund the additional costs of operations. In 2004/05, the MoD received £1.1 billion to fund the costs of operations in Afghanistan, Kosovo and Iraq. By 2008/09, this total had risen to £4.5 billion.

These measures have ameliorated, but not fully compensated for, two important sources of strain on the budget. First, the costs of the equipment programme have risen, and defence decision-makers have found it increasingly difficult to meet existing commitments. Attempts to delay costs by pushing programmes to the right have allowed temporary savings, while often increasing eventual total costs. Yet, in the case of the MoD's largest current programme, the Typhoon aircraft, the attempt to reduce the UK order has run aground, as a result of which the solvency of the overall budget will soon depend on the MoD being able to sell a large proportion of its latest aircraft as soon as possible after they have been acquired.

Secondly, the experience of continuing operations since 2003 has led to a debate on whether the priorities set in 1998 need to be updated to account for subsequent international and technological changes. Even as the government continues to invest a large part of the resources devoted to air power to purchasing Typhoon, for example, UK forces in Afghanistan remain much less well-equipped with helicopters than their US allies. The rapidly evolving character of warfare is also generating demands for a wide range of new capabilities, many of which did not even exist in 1998.

The 'New Chapter', published four years after the SDR, in July 2002, was an attempt to update the findings of the SDR, taking into account the new priorities of the post-9/11 world. Yet it still reflected the assumption, confirmed by Kosovo and Sierra Leone, that an initial period of intense fighting can be expected to give way rapidly to a peacekeeping phase. It could not take into account the subsequent, and much more difficult, experience of Iraq and Afghanistan. As a result of these operations, pressures to maintain legacy programmes and capabilities have come increasingly into conflict with demands to respond to the lessons of operational experience. The July 2004 *Future Capabilities* White Paper did make some significant steps towards a more flexible force structure, and was seen by some as being a 'de facto second QDR'.[5] Since then, however, there has been no further major review of defence priorities.

The completion of withdrawal from Iraq in summer 2009, together with the worsening fiscal situation, has increased the pressure for a new and comprehensive reflection. With less than a year to go

before the next General Election, the government probably no longer has the time left in which to complete such a review. But it could still initiate the preparatory studies that will be needed to ensure that such an exercise can be conducted in as efficient and timely a manner as possible.

When a review does come, how might the MoD fare in the competition for resources? Leaders of all major political parties recognise the key role that the armed forces play in supporting national security. They are also aware that public support for the country's servicemen and women is as strong as ever, and this has been reinforced by the bravery and skill with which they have fulfilled the difficult missions they have been given in recent years.

Yet politicians also know that this strong level of support for the armed forces has been accompanied by an intensification of controversy over defence policy and operations. From its inception, the Iraq intervention was bitterly controversial. It remains so. Many also question whether success in Afghanistan is possible on a realistic timeframe and, even if it is, whether the gains made will justify the growing toll of British casualties. For some, the new requirements created by these operations provide a compelling argument for more resources to be devoted to defence. For others, however, they reinforce the view that the country's interests would be better served by a more selective approach to the commitment of Britain's armed forces.

Certainly there appears to be relatively little public sympathy, outside those directly involved in the defence sector, for protecting the MoD from the coming period of austerity. With the exception of the early 1980s, the budgetary priority given to defence has been falling since the end of the Korean War, as it has in most of the UK's European allies. Even the UK's involvement in Iraq and Afghanistan, two of the most sustained and expensive deployments of the post-1945 period, has only slowed this long-term trend.

The New Austerity: How Deep will the Axe Cut?

The core defence budgets for 2009/10 and 2010/11 have already been set, and are unlikely to be substantially altered. But, in the immediate aftermath of the next election, most analysts now expect there to be a comprehensive review of government commitments, leading to a prolonged period of austerity in public spending, starting with fiscal year 2011/12.

Plans announced in the 2009 budget assume that total real government spending will fall by 0.1 per cent per annum in the three years to 2013/14. It is also expected that a low rate of spending growth – perhaps around 0.5 per cent per annum – will have to be

sustained for the 2013-2016 Spending Review period.[6] The costs of paying interest on the national debt are set to rise rapidly (at 8.4 per cent annually, according to an Institute for Fiscal Studies estimate), and will have to be met from this total. Social security obligations will also rise at around 1.8 per cent per annum, in the absence of cuts in benefit eligibility or levels. On these assumptions, other departmental spending is due to fall by 2.3 per cent per annum in real terms during 2010-2013, with a further reduction during 2013-2016.[7]

The government emphasises that a large part of its planned reduction will take the form of cuts in the capital budget, which has seen a rise in net investment in new public infrastructure (hospitals, schools, railways, roads, prisons, etc.) from 0.6 per cent of GDP in 1997-98 to 3.1 per cent of GDP in 2009-10, and is now due to fall to only 1.3 per cent of GDP by 2013-14.[8] As a result, it argues, current spending will continue to grow (albeit slowly) in real terms.

Yet this should not be a source of comfort for MoD planners. Of all the big departments, the MoD is one of the most investment-intensive, with £9 billion of planned capital spending in 2009/10, equivalent to 16 per cent of total government spending.[9] Moreover, MoD capital spending rose by 33 per cent in real terms between 2003/04 and 2009/10, compared with an increase of only 7 per cent in the resource budget.[10] If the new chancellor persists in focusing cuts disproportionately on the capital budget, therefore, the MoD could be one of the hardest-hit departments. If the MoD's current and capital budgets are reduced in line with those planned for the whole government (excluding interest payments and social security), total defence spending would fall by an estimated 6.8 per cent in real terms between 2010/11 and 2013/14.[11] The estimated reduction over the six years to 2016-17 would be 11 per cent in real terms.

If the MoD succeeds in obtaining an exemption from the full impact of the planned cuts in the capital budget, the extent of these reductions could be less severe. If such a concession were to be made to the MoD, however, it could face pressure from another source. In the calculation above it is assumed that the MoD will be able to obtain a budgetary settlement comparable to the average of all other spending departments. Yet, as already discussed, this is something which it has not been able to achieve since the early 1980s, the high point of concern over renewed Soviet expansionism.

It remains possible that a new defence secretary, in a new government, will be able to convince his (or her) Cabinet colleagues that the armed forces have been underfunded for so long that other departments should now take a greater share of the load. After all,

it can be argued, they have all benefited from the 'peace dividend' that defence budget cuts have released since the mid 1980s.

Yet the armed forces would be ill-advised to assume that such an outcome were likely, as a brief consideration of the situation in competing spending departments indicates:

- A new government may be willing to contemplate reducing some of the social security commitments made by the current administration, for example by ending winter fuel allowances for pensioners, abandoning the commitment to re-index the state pension against earnings from 2012, introducing means-testing for child benefit, and reducing tax credits for middle-income families. Yet levels of public pension provision in the UK are already amongst the lowest in the OECD. Numbers of old people are rising, and increasing unemployment could push up the bills for unemployment and disability benefits above current plans. It may be possible to slow the growth in spending in this sector, but only if the government is willing to incur substantial political pain from those who will lose as a result.

- Any incoming government will need to make increased efforts to find economies in the NHS, whose budget has grown at an unsustainable rate over the last decade. Yet so far, politicians from both parties have done little to prepare the public for this, instead stressing that the NHS remains their highest spending priority. Given the demographic and political pressures for increased provision, even a reduction in the medium-term rate of spending growth to 2 per cent per annum would be more than has been achieved since the 1970s. Achieving a real reduction in NHS spending is probably beyond the limits of political feasibility.

- Spending on public order and justice (police, prisons, courts, etc.) may be a more tempting target. The UK now spends much more in this area than other EU countries. Yet some argue that the rapid increase in spending since 1980 has not been matched by increased efficiency. On the other hand, the increased levels of property crime that seem certain to be one of the results of the coming recession are going to make it even more difficult to reduce the number of police officers or prison residents. Spending on public order and safety has already risen from the equivalent of 42 per cent of defence spending in 1987/88 to the equivalent of 91 per cent in 2008/09. The MoD will find it hard to argue that this trend should now be reversed, and that security at home should be cut in order to maintain capabilities for intervention abroad.

One could go on. The reality is that the relatively low ranking of the MoD in government spending priorities reflects long-standing political preferences, dating back to the 1950s, and intensified since the end of the Cold War. These preferences could change, especially if military threats to the UK were to re-emerge. In the absence of such a contingency, however, the MoD will struggle to limit any cuts it is asked to make to the average level sought for other departments.

Even if the only sectors that are given special treatment are health and education, and equal misery applies to all other departments, the impact on the MoD would be severe. Assume, for example, that the health and education budgets are frozen at 2010 levels in real terms, and that the rate of growth in social security spending is reduced to 1 per cent per year. This would leave the rest of government, including the MoD, facing a cut of 14 per cent in their budgets over the period 2010-16.

It is entirely plausible that, faced with the combined protestations of spending departments, a new chancellor could be forced to concede a lengthening of the timetable for spending reductions established in the 2009 Budget. It is also likely that a significant part of the fiscal adjustment will have to be met, at least in the short term, through tax increases.

In the light of all these competing pressures, the best estimate is that the MoD will be required to make a real terms budget reduction over the period 2010-16 of around 10-15 per cent. If tax increases are introduced in order to share the burden of fiscal adjustment, the level of this cut could be reduced. If, on the other hand, the government decides to provide even a modest level of real terms growth to health and education, or if the economy fails to recover its previous trend rate of growth by 2010, even tax increases may not be able to prevent even deeper defence spending reductions.

1964 Revisited?

Parallels for the current financial crisis are sometimes drawn with the 1976 crisis, in which the UK was obliged to seek a $4 billion loan from the IMF, as well as accepting a freeze on public spending at 1976-77 levels. In practice, after a temporary slowdown, government spending continued to rise, with defence recording a 17 per cent real increase between 1975-76 and 1985-86, and health increasing by 32 per cent.[12]

A more plausible parallel, at least for the defence budget, may be with the experience of the 1964-1970 Labour government. Coming to power in 1964 after thirteen years in opposition,

the new government soon discovered that inherited plans for defence would require annual real growth in spending of 4 per cent. It quickly decided that this was unaffordable, given its other priorities, and decided to limit the level of defence spending for 1970-71 to the level of 1964-65. At first, it was unprepared to take all the decisions necessary to meet this target, given the continuing military operations in Aden and Malaysia. Instead, the next three years saw a sequence of separate decisions – making sharp cuts in the aircraft R&D budget, evacuating Aden, cancelling the carrier programme, and then, during the devaluation crisis of late 1967, agreeing the final withdrawal from Singapore and Malaysia – that cumulatively allowed the 1970 spending target to be met. Even then, as a result of the offsetting cost increases for the UK's conventional contribution to NATO (notably the British Army on the Rhine and RAF (Germany)), total defence spending fell by only 4 per cent over the period.[13]

Half a century later, the constraints on overall spending growth are greater than they were in 1964, but defence is a less important part of the total picture. Yet many aspects of the 2010 problem would be recognisable to Britain's then new ministers, as they gathered in Chequers to review defence policy options. Now, as then, they faced a need to impose financial discipline on an overcommitted defence programme. At the same time, the requirement to reduce military commitments could not easily be fitted within the timetable of Treasury deadlines. While agreeing the overall budget path for defence at the very beginning of Labour's period in office, therefore, the process of establishing a clear sense of priorities – and, in particular, the eventual decision to prioritise NATO and nuclear commitments at the expense of those in the Middle East and Asia – only emerged incrementally, as opportunities arose for disentanglement from existing commitments and programmes. Such a procedure may yet prove to be the least suboptimal way for the government to implement the defence reductions that now seem probable over the next six years.

Finding Savings

So where might those charged with conducting the 2010 Defence Review look when seeking to meet these challenging targets for savings? What follows are emphatically not intended to be the author's own recommendations. But some of these ideas will probably have to be adopted if the MoD is to balance its books. After many years of efficiency savings within a slow-growing budget, there are few easy pickings left that can deliver large, but pain-free, savings.

Operations

One possible target for savings will be the additional costs of military operations, up to now funded from the Treasury Reserve, and amounting to £4.5 billion in 2008-09. The level of total operational costs should fall significantly in 2009/10 and 2010/11, with the completion of the Iraq operation (the cost of which reached its highest level, of £1,958 million, in 2008/09). But the costs of operations in Afghanistan continue to rise, from £199 million in 2005/06 to £738 million in 2006/07, £1,504 million in 2007/08, and £2,559 million in 2008/09. During early 2009, the prime minister and Treasury resisted MoD requests for a further permanent increase in the number of troops based in Afghanistan. Even so, the fast-developing nature of the threat faced by UK forces means that it may prove difficult to reduce Afghanistan operational costs below current levels.

The UK can plausibly argue that it is contributing much more than any other US ally to the Afghanistan operation. Given this, the US 'surge' into Helmand and Kandahar provinces could be used to relieve the pressure for further increases in the UK's own forces. There is also, in any case, a strong military argument for much greater operational integration between US and UK forces in the field. Such integration may yield some useful financial savings.

For serious savings to be made in Afghanistan costs, however, the government would have to seriously consider a radical scaling-down of the UK military presence in the country. The conditions for this clearly do not exist at present, and a unilateral UK drawdown would have considerable costs for UK/US relations. Yet it is a possible source of savings over the years to 2016, the likely period of the next Defence Review.

As in the case of UK commitments in the Far East in 1964-70, the dynamic of the process that might lead to such a withdrawal does not lend itself easily to the processes inherent in a one-off Defence Review. Yet it is still entirely possible that, at some stage during this period, the conditions for a useful UK (or indeed US) combat presence will no longer exist, and an honourable transition to a support role will become possible. At the margins, increasing financial stringency at home may give UK leaders a further reason to restrain the continuing costs of the operation (in both human and financial terms), while also seeking solutions that allow such an exit to take place. This pressure will increase to the extent that the Treasury insists on the MoD funding part of the additional operational cost from its own core budget. But it will be developments within Afghanistan itself (including the success of Taliban reconciliation efforts and the strengthening of local security forces), together with strategic decisions taken in Washington DC, that will be the most important drivers of UK withdrawal.

Yet it is unlikely that the MoD will be able to count reductions in operational costs for Afghanistan against any savings targets set for it by the Treasury in the next Spending Review. Since these costs have been met from the reserve, the Treasury will resist incorporating them in a new MoD 'core budget', especially if there is agreement that the MoD will be able to access the Reserve again in order to fund the extra costs of future major operations.

Pay

Personnel costs, including pension contributions, cost the MoD around one third of total defence spending. Three-quarters of this (or £9.1 billion) is for the costs of military personnel, and the remainder (£2.8 billion) pays for the MoD's civilian personnel.[14]

Pay and pension conditions in the public sector as a whole have recently improved relative to those in the private sector, especially in light of the impact of a declining stock market on private pension schemes, and the consequent greater attractiveness of public sector pensions. Moreover, rising unemployment is making alternative employment in the private sector a less appealing alternative for MoD personnel. Indeed leaving rates are now falling so rapidly that active efforts may soon be needed to curb recruitment, in order to avoid service numbers exceeding planned levels. In these circumstances, a new government, faced with the scale of the country's fiscal deficit, might want to look at the contribution that across-the-board public sector pay restraint could make to its overall saving targets.

This may be particularly difficult for armed forces personnel, whose pay is based on recommendations from the Armed Forces Pay Review Body (AFPRB). No government has refused to accept AFPRB recommendations since its establishment in 1971, except to phase their implementation. In recent years, however, the AFPRB has recommended, and the government has accepted, increases in armed forces pay that are significantly above the levels for which the MoD had allowed in its financial planning. The 2008 Review led to additional annual costs of £109 million above planning assumptions. Similarly, the recommendations of the 2009 Review increased the pay bill by 3.4 per cent, well above the 2.5 per cent planning assumption, thereby incurring £80 million in annual additional costs.[15]

Persuading the AFPRB to accept a reversal of this trend could yield significant savings. For example, were pay to be reduced below planned levels by 5 per cent – which could be achieved without cuts in nominal pay, given continuing inflation – annual savings by 2016 on personnel costs would amount to around £600 million, equivalent to around 1.5 per cent of total defence spending. A

saving of this magnitude could provide a useful contribution to the overall target for budgetary reduction. Whether it becomes possible, however, depends on the Government's overall pay policy for the public sector.

Procurement

An examination of the size and shape of the procurement budget has been a central feature of most past reviews, and is now becoming central to public discussion of the options for the next review. In the short term (one to two years), the scope for savings on major procurement projects may be relatively limited, given an overhang of outstanding contractual commitments amounting to some £18 billion.[16] Within these constraints, the proportion of the forward equipment programme that can be cancelled or reallocated, with relatively little financial penalty, increases steadily in each successive year.

As a result, some of the most commonly discussed options for review-related savings are proposals for the cancellation, or postponement, of major equipment projects. But some of these ideas do not take sufficient account of the degree of contractual obligation involved. For example, gross spending on the eighty-eight aircraft to which the UK is committed as part of the third tranche of the Typhoon project could amount to as much as £1 billion per annum during some of the peak procurement years of 2012-16: probably the MoD's biggest single procurement commitment during this period. Although the government has not finally committed to taking the full number, it faces the prospect of paying such large penalties to its project partners if it does not that it is likely to be more cost-effective to go ahead with the procurement, and then sell or cannibalise a large proportion of the aircraft.

Other large projects are less well-advanced than Typhoon, or have less restrictive contractual arrangements. Thus, for example, programmes for two new aircraft carriers and their associated F-35 aircraft, four new ballistic missile submarines and the Future Surface Combatant could all (in principle) be postponed or reduced in size. Postponement of the new *Vanguard*-replacement submarines could be particularly tempting, given that this project is currently due to replace Typhoon as the MoD's largest single procurement project, with annual costs due to reach as much £1 billion in the period from 2016/17 onwards.[17] Recent reports of cost escalation for the Royal Navy's new carriers – due to be the biggest and most powerful surface warships ever constructed in the UK – may also prompt another look at this programme.

In each of these cases, strong military and industrial arguments can be presented against the postponement of major programmes that

are, especially in the case of the carriers, already well advanced. Given the extent of the likely budgetary requirement, however, all are likely to be subject to a rigorous examination in the Defence Review.

Capabilities

Yet the savings available from postponing the introduction of new equipment can only be temporary if it does not also lead to the elimination of the operational requirement that it is intended to meet. Capital expenditure on equipment in 2007/08 totalled £5.4 billion, equivalent to 14 per cent of total defence spending. A further £2.7 billion (or 7 per cent of total spending) was spent on research and development.[18] But around three-quarters of the defence budget is spent on maintaining existing capabilities, including personnel costs, equipment repair and maintenance, transport and building management. Where purchase of new equipment allows running costs to be reduced (for example by rationalising support facilities or reducing deployed numbers), it can save money. Previous reviews, including the 2004 *Future Capabilities* mini-review, have focused as much, if not more, on capabilities as on new equipment in isolation. The next review is likely to do the same.

The review will therefore have to look again at whether further reductions should be made in the numbers and types of aircraft squadrons, naval vessels and/or ground force formations, together with their associated support facilities. It will also want to examine whether there are capabilities that need to be increased, both in response to recent operational experience (for example, requirements for tactical and strategic transport) and new technological opportunities (for example, in relation to unmanned vehicles and cyber-warfare).

The continuing debate on the appropriate balance in UK force planning between preparing for major inter-state warfare and for fighting intra-state 'wars among the people' is relevant here. Above a certain limited scale of operations (e.g. Sierra Leone), the UK is only likely to be involved in either type of warfare if it is part of an international coalition, usually led by the US. Much of the debate on UK defence priorities, therefore, is fundamentally about how its armed forces can provide the most effective contribution to collective efforts, even as a capability for meeting uniquely national requirements (for example in Northern Ireland) has to be maintained.[19]

Assessing the balance between these different types of contributions depends, in part, on where future collective operations, in which the UK believes it to be in its interests to participate, would take place.

The recent focus of UK policy has been on conflicts in South-West Asia and the wider Middle East, and to a lesser extent sub-Saharan Africa, all regions where the risks of major power warfare are currently assessed to be relatively low.[20] To the extent that the UK wanted to shift focus to East Asia, however, the case for prioritising capabilities for high-tech maritime warfare could be increased, as it has been in the most recent defence review in Australia, which is increasing its investments in anti-submarine warfare capability.

Were the Defence Review to decide that the UK should focus its efforts on deepening its comparative advantage in stabilisation and counter-insurgency, by contrast, capabilities for large-scale maritime warfare would likely lose out to the sort of capabilities that have often been in short supply in Iraq and Afghanistan: attack helicopters, tactical and strategic transport, surveillance and intelligence assets, trainers, special forces and engineers, as well as greatly enhanced civilian capabilities. There may be more debate about how far such a focus also requires heavy-footprint infantry forces, as against the more indirect approach favoured by some counter-insurgency specialists.[21]

It is important that these debates should not be seen primarily through the prism of inter-service rivalry. Indeed some of the fiercest debates are likely to be between different branches of the same services. Nor is it the case that capabilities for counter-insurgency and major war are always mutually exclusive. The continuous process of operational improvement which the armed forces are now experiencing as a result of the challenging conditions of Iraq and Afghanistan may actually be one of the best ways of developing the individual and organisational capacities that will be needed were the need for major-war mobilisation to re-emerge in ten or twenty years time.

What is clear is that, given the extent of savings that are likely to be required in the next Defence Review, not all existing capabilities – far less legitimate aspirations for new capabilities – can be afforded. A moment of choice for British defence decision-makers, as significant for its foreign policy as the decision to withdraw from East of Suez in the 1960s, is fast approaching.

Malcolm Chalmers *is Professorial Fellow in British Security Policy at RUSI. He is also Professor of Defence and Foreign Policy at Kings College, London, and Professor of International Politics at the University of Bradford. He was previously Special Adviser to Foreign Secretaries Jack Straw MP and Margaret Beckett MP.*

Notes

1 Organisation for Economic Co-operation and Development, *OECD Economic Outlook*, Number 85, June 2009, p. 252.

2 For a useful analysis of the Strategic Defence Review, see Colin McInnes, 'Labour's Strategic Defence Review', *International Affairs*, (Vol. 74, No. 4, 1998), pp. 823-845.

3 This calculation takes into account £147 million of spending on Bosnia and £14 million spending on Kosovo during 1998-99. *House of Commons Hansard Written Answers*, 2 May 2000. Operations spending during 2008/2009 included £2,559 million for Afghanistan, £1,958 million for Iraq and £19 million for the Balkans. 'Further memorandum from the Ministry of Defence' in House of Commons Defence Committee, *Spring Supplementary Estimate 2008-09,* HC 301, March 2009, p. 7.

4 Calculated for the period from 1983-84 to 1990-91. HM Treasury, *Public Expenditure Statistical Analyses 1999-2000*, Cm 4201, March 1999.

5 MoD, *Delivering security in a changing world: Future Capabilities*, The Stationery Office, July 2004. The reference to the QDR is from Paul Cornish and Andrew Dorman, 'Blair's wars and Brown's budgets', from Strategic Defence Review to strategic decay in less than a decade', *International Affairs*, 85, 2, 2009, p. 253.

6 Martin Wolf, 'Tackling Britain's fiscal debacle', *Financial Times*, 7 May 2009.

7 Gemma Tetlow, 'Public Spending', *Institute for Fiscal Studies Budget Briefing*, 23 April 2009.

8 HM Treasury, *Budget 2009: Building Britain's Future*, The Stationery Office, April 2009, pp. 115, 128.

9 HM Treasury, *Public Expenditure Statistical Analyses 2009*, Cm 7630, June 2009, Table 1.11. By comparison, it accounts for only 6 per cent of total government expenditure. *Ibid*., Table 4.3.

10 *Ibid*., Tables 1.6, 1.11.

11 Assuming a reduction of 25 per cent in total (and MoD) capital spending and a reduction of 2.4 per cent in total (and MoD) current spending, the latter excluding AME and debt interest payments.

12 Christopher Hood, Carl Emmerson and Ruth Dixon, *Public Spending in Hard Times*, Institute for Fiscal Studies, 2009.

13 Saki Dockrill, 'Britain's Power and Influence: Dealing with Three Roles and the Wilson Government's Defence Debate at Chequers in November 1964', *Diplomacy and Statecraft*, 11, 1, March 2000, pp. 211-240.

14 MoD, *UK Defence Statistics 2008*, The Stationery Office, 2008, Table 1.3.

15 *Armed Forces' Pay Review Body: Thirty-Eighth Report 2009*, Cm 7156, The Stationery Office, March 2009, p. 7.

16 MoD, *Annual Report and Accounts 2007-2008 Volume 1*, The Stationery Office, 21 July 2008, p. 216. Options are also limited by rising levels of long term Private Finance Initiative service contracts, amounting to some £1.3 billion per annum in 2007-08 and on a rising trend. Of this total, only £300 million consists of contracts that are due to expire within five years. Ibid., p.318.

17 Malcolm Chalmers, 'Britain's New Nuclear Debate: A Credible Road Map for Disarmament?', *RUSI Journal*, 154, 2, April 2009, pp. 34-41.

18 Compared to total defence spending of £37.4 billion. MoD, *UK Defence Statistics 2008*, The Stationery Office, 2008, Tables 1.1, 1.4.

19 For further discussion, see Malcolm Chalmers, 'A Force for Influence: Making British Defence Effective', *RUSI Journal*, 153, 6, December 2008, pp. 20-27.

20 Cabinet Office, *The National Security Strategy of the United Kingdom: Security in an interdependent world*, Cm 7291, March 2008, p. 40.

21 For example, see David Kilcullen, *The Accidental Guerrilla*, Hurst Publishers, 2009, especially pp. 285-287.

Future Defence Review Working Papers

Editor: Michael Codner

Royal United Services Institute for Defence and Security Studies
Whitehall, London SW1A 2ET, UK

Tel: +44 (0) 20 7747 2600
Fax: +44 (0) 20 7321 0943

The views expressed in FDR should not be taken to represent a corporate view of RUSI.

E-mail: michaelc@rusi.org
Web: www.rusi.org/fdr

All RUSI FDR Working Papers are the copyright of RUSI and may not be copied, reproduced or electronically transmitted in any form without prior permission from the Institute.